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IN THE HIGH COURT OF GUJARAT AT AHMEDABAD

INCOME TAX REFERENCE No 27 of 1984

For Approval and Signature:

Hon'ble MR.JUSTICE R.K.ABICHANDANI and
MR.JUSTICE R.BALIA.

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1. Whether Reporters of Local Papers may be allowed to see the judgements?-Yes.

2. To be referred to the Reporter or not?-Yes.

3. Whether Their Lordships wish to see the fair copy of the judgement?-No.

4. Whether this case involves a substantial question of law as to the interpretation of the Constitution of India, 1950 of any Order made thereunder?-No.

5. Whether it is to be circulated to the Civil Judge?-No.

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COMMISSIONER OF INCOME TAX

Versus

SARASPUR MILLS LTD.,

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Appearance:

Mr.M.J. Thakore, Advocate, instructed by MR MANISH R BHATT for the Applicant.

SERVED BY RPAD for the Respondent.

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CORAM : MR.JUSTICE R.K.ABICHANDANI and
MR.JUSTICE R.BALIA.

Date of decision: 05/02/97

ORAL JUDGEMENT : (Per R. Balia, J.)

On the application of the Commissioner of Income

Tax under Section 256(1) of the Income Tax Act, 1961, following two questions of law arising out of its order in ITA No.835 of 1982 for the assessment year 1980-'81 have been referred to this Court for its opinion along with the statement of the case :-

1. "Whether, on the facts and in the circumstances of the case, the Tribunal was right in law in coming to the conclusion that the cash payment of house rent allowance did not form part of salary for the purpose of section 40A(5) of Income-tax Act, 1961?"

2. "Whether, on the facts and in the circumstance of the case, the Tribunal was right in law in allowing extra shift allowance on exhaust fans forming part of textile machinery notwithstanding the fact that item III(iv) of Appendix-I of the Income-tax Rules 1962 specifying rates of depreciation specifically excluded fan installations from E.S.A?"

The assessee is a Company. It paid by way of cash house rent allowance to its employees during the previous year relevant to the assessment year in question, amounting to Rs.15,337/-. Since extent of deduction on account of salaries being paid to its employees for the purposes of computing the profits and gains arising out of its business is inhibited by the provisions of Section 40A(5) of the Act, the Income Tax Officer included this sum in determining the amount of salaries paid to its employees for the purposes of finding out the extent to which the expenditure on account of salaries are to be disallowed under the aforesaid provisions. The assessee contested the case of the Assessing Officer on the ground that such cash allowances are not to be considered as `salary', or `perquisite', within the meaning of Section 40A(5) read with Explanation thereto which determines the meaning of salary and perquisite for the purposes of the section. Sub-section (5) speaks about expenditure assessee incurs, which results directly or indirectly in the payment of any salary to an employee or a former employee, or incurs any expenditure which results directly or indirectly in the provision of any perquisite whether convertible into money or not to an employee or incurs directly or indirectly any expenditure or is entitled to any

allowance in respect of any assets of the assessee used by an employee either wholly or partly for his own purposes or benefit, then, such expenditure beyond the limit prescribed under the sub-section are not to be deducted in computing profits and gains of business of the assessee. The scheme of the Act makes it clear that such expense must either result in payment of salary or in the provision of any perquisite whether convertible into money or not or entitlement to any allowance in respect of an asset of the assessee used by an employee for his own purpose or benefit. Therefore, unless the cash allowance paid to an employee falls in any of the categories, viz., salary, perquisite, or allowance for the use of assessee's assets for the benefit or purposes of the employee, the same cannot be considered for the purposes of determining the ceiling of expenses to be excluded from allowance. For the purposes of the said sub-section, the Act itself has provided the ambit and scope of expenditure which is to be considered as salary or perquisite in Explanation 2.

It is nobody's case that the cash payment as house rent allowance is made to the assessee in respect of any accommodation made available by the assessee for the use of its employees. Explanation 2 defines `salary' to mean as defined in clause (1) read with clause (3) of Section 17 by omitting perquisites and amounts referable to the contributions to the recognised provident fund to the extent the same are chargeable to tax. Section 17 defines `salary', `perquisite' and "profits in lieu of salary". While sub-section (2), which defines `perquisite', has been excluded from consideration for the purposes of Section 40A(5), the expenses incurred on salary by an employer has to be determined with reference to the provisions of Section 17 by determining whether the same are includible in the term `salary' and "profits in lieu of salary", within the meaning of that Section. It may also be noticed that Section 17(1) is an "inclusive definition" of the term `salary' and is indicative of the fact that it is not an exhaustive definition so as to exclude what ordinarily would fall within the meaning of `salary'.

According to Section 17, `salary' includes wages, as well as any fees, commissions, perquisites or profits in lieu of or in addition to any salary or wages. In terms of sub-clause (iv) of sub-section (1), while `perquisite' has been separately defined in sub-section (2), "profits in lieu of salary" in addition becomes subject matter of sub-section (3). The fact that the statute defines `salary', which includes wages and other

things and also includes any fees, commissions, perquisites or profits in lieu of or in addition to any salary or wages, further indicates that the word salary is of wider import than wages simpliciter as ordinarily understood. Even in ordinary sense, the term `salary' denotes the whole of remuneration payable for the services rendered or the work done. It will be apt to refer to the opinion of Fry L.J., in Re. Shile ex p Shine (1892)1 QB 522 as to what is meant by `salary' :-

" ... Whenever a sum of money has these four characteristics first, that it is paid for services rendered; secondly, that it is paid under some contract or appointment; thirdly that it is computed by time; and fourthly that it is payable at a fixed time - I am inclined to think it is salary ---- I do not mean to say that that is complete definition of salary; but I think that wherever these four circumstances concur, the payment is salary...."

According to New Shorter Oxford English Dictionary,

"... Any cash, fee or remuneration additional to normal salary or revenue to an office or post, office or position, a benefit incidental to a particular employment is a part of salary...."

If we consider from this aspect, obviously in the context in which we are required to consider this question, unless any benefit or payment can be said to be a perquisite, if it has the characteristics as referred to by Fry Lord Justice, would be included in the term `salary' itself.

As we shall presently see, the house rent allowance paid in cash does not form part of the term `perquisite'. However, if it is paid by the employer to employee as the terms and conditions of employment for services rendered and it is payable periodically computed in terms of time per month and is not a result of anything but arising out of relationship of employer and employee in terms of the contract, it must be considered as `salary' itself. Even otherwise, when the inclusive definition of `salary' includes any profits in addition to any salary or wages, any allowances or extra payments, whether for rain clothes given to its employees, lodging allowances, trade union allowances, city compensatory

allowances, etc., are to be included in salary as "profits in addition to salary".

In this connection, it will also be relevant to notice that Chapter III provides "incomes which do not form part of total income" and Section 10 makes provision for "incomes not included in total income". Sub-section (13A) exempts special allowance specifically granted to an assessee by his employer in respect of residential accommodation occupied by the assessee to such extent as may be prescribed to be exempt from being included in the income of the employee. By necessary implication, it means that the cash payment in respect of house accommodation beyond exemption limit is to be included in `salary' under Section 17. If the house rent allowances were not to form part of `salary', `perquisite' or "profits in lieu of or in addition to any salary or wages", there would have been no occasion for providing this exemption. It is beyond the pale of doubt that whatever is described not to be included in Section 10 presupposes that but for the said provision, it is an income chargeable to tax under various heads under the Act. As Section 10(13A) deals with an allowance granted to an assessee by his employer, it refers to income to be computed under the head `salary'. We are, therefore, of the opinion that the cash payment of house rent allowance does form part of `salary', as defined under Section 17(1) read with Section 17(3) for the purposes of Section 40A(5) of the Income Tax Act, 1961.

In our conclusion that cash payment for house rent allowance forms part of `salary', we are fortified by the decisions of Delhi High Court in C.I.T. v. Shriram Refrigeration Industries Ltd., 197 ITR 431, of Andhra Pradesh High Court in M. Krishna Murthy & others v. C.I.T., 152 ITR 163 and of Karnataka High Court in Karnataka Electricity Board Employees' Union v. Union of India, 179 ITR 521.

Sub-clause (b) of Explanation 2 defines `perquisite' for the purposes of the sub-section. Sub-clauses (i), (ii) and (iii) obviously can have no application to the expenses incurred in cash as the same refer to the accommodation or benefit or amenity granted or provided free of cost or at a concessional rate to the employee by the assessee. Therefore, condition precedent for invoking sub-clauses (i), (ii) and (iii) is making some provision in some form otherwise than in cash, value of which alone is to be considered, whether full or concessional, to the extent it has been provided to the assessee. The expression `whether convertible into money

or not' also indicates that perquisites are ordinarily referable to valuation of something provided to an employee not in terms of money, though the employer may incur actual expenditure on it. Sub-clause (v) also does not cover such cash payments, as it deals with payment to effect an assurance on the life of the employee or to effect a contract for an annuity other than a recognised provident fund or an approved superannuation fund. The only sub-clause, which Revenue could call in its aid, remains sub-clause (iv) of clause (b), which reads as under :-

> "...(iv) payment by the assessee of any sum in respect of any obligation which, but for such payment, would have been payable by the employee;...."

Obviously, this refers to payment made by the assessee to some other party, to whom the employee owes an obligation to pay. It does not refer to any payment made to the employee itself irrespective of the fact whether it is to discharge any existing obligation of the employee or even on the conditions that any such obligation at all exists.

In our reading of the aforesaid provision, we are fortified by the decision of the Supreme Court in Commissioner of Income-Tax v. Mafatlal Gangabhai and Co. (P) Ltd., 219 ITR 644. The Supreme Court was called upon to consider whether the cash payments made by the assessee to its Directors / employees, such as House Rent Allowance, Conveyance Allowance, Furniture Allowance, etc., should be considered as `perquisites', within the meaning of Section 40(a)(v) of the Income Tax Act, 1961 or under Section 40A(5) of the Act, with which we are concerned. Negativing the contention of the Revenue that the same should be held as `perquisites', the Supreme Court held that the payments by an assessee to his / its employees do not fall within the ambit of Section 40(a)(v) or Section 40A(5)(a)(ii), as the case may be. It may be noted that under Section 40(a)(v), reference to any expenditure resulting directly or indirectly in the provision of any benefit or amenity or perquisite, whether convertible into money or not, to an employee, to the extent such expenditure or allowance exceeds one-fifth of the amount of salary payable to the employee, was to be disallowed while computing the profits and gains of business or profession. Section 40A(5)(a)(ii) refers only to perquisite. Therefore, the disallowance under Section 40(a)(v) was confined to

benefits or amenities or perquisites, but did not include salaries other than those paid to the employees. Under Section 40A(5)(a)(i), the expenditure referred to is payment of any salary to an employee or a former employee by the assessee and sub-clause (ii) refers to expenditure, which results directly or indirectly in the provision of any perquisite (whether convertible into money or not), to an employee. In that regard, the need for determining the allowable and non-allowable expenditure incurred by the assessee for payment of salary and perquisites to the employees is widened. Noticing this distinction between the two provisions, though the question whether the cash allowance forms part of salary or not was not before the Court, it opined :-

> "... These cash payments will, of course, be treated as salary paid to the employees and will be subject to the limits / ceiling, if any, in that behalf. But they cannot be brought within the purview of the words "any expenditure which results directly or indirectly in the provision of any benefit or amenity or perquisite"-more so because of the following words "whether convertible into money or not"...."

It has also to be noticed that the decision has been confined to the provisions of Section 40(a)(v) or Section 40A(5)(a)(ii).

As a result of aforesaid discussion, we answer question No.1 referred to us in the negative, i.e. to say, in favour of Revenue and against the assessee.

The second question concerns the allowability of a claim to extra shift allowance for the purpose of computing the allowable depreciation on the exhaust fans, which was rejected by the assessing authority on the ground that as per the provisions contained in Appendix I read with Rule 5 of the Income Tax Rules, 1962, specifying rates of depreciation, extra shift allowance has been specifically excluded on fan installations at any place of business or establishment. The assessee's claim was founded on the premise that the exhaust fans fitted in the factory premises are part of textile machinery and, therefore, cannot be considered as electrical machinery as given in Appendix I of the Income Tax Rules. C.I.T. (Appeals) also rejected the contention of the assessee in that regard. However, it found favour with the Tribunal. It found that :-

"... In a textile mill the purpose of installing exhaust fan would be to ensure certain level of temperature in the factory premises where various processes are undertaken. The working of the machinery as also the non-climatic condition will have an impact on the heat generated in the atmosphere and, therefore, the atmosphere within the factory shed would become acceleratingly hot. To keep the heat and the moisture in the atmosphere at desired level so as not to adversely affect quality of cloth or yarn, exhaust fans are installed in the factory premises and that is why sometimes the exhaust fans are accompanied by the blowers which are installed at the bottom of the factory premises so as to bring within the factory shed cool air solely for the purpose of conditioning the air at the desired level. The function of the exhaust fan is to suck out hot air lying at the highest layer of the atmosphere within the factory shed so that cool air can constantly blow in within the factory shed...."

It made reference to the distinction between the exhaust fans and office fans and held that the exhaust fans are machinery and forms part of textile machinery when they are installed in factory premises. This Court had an occasion to consider a like question whether air-conditioners, which were held to be necessary requirement for process of crimping artificial silk yarn in the factory manufacturing artificial silk yarn, ought to be treated as part of a plant or machinery of the artificial silk manufacturing or is to be treated independently as air-conditioning machinery used for artificial silk manufacturing machinery/plant, in ITR 346 of 1983, decided on 4th December, 1996. The court reached the following conclusions :-

(1) Under the scheme of the statutory provision, each apparatus conforming to the definition of `machinery' or `plant', as the case may be, has to be taken individually for the purpose of considering computation of depreciation and not the organisation or the unit as a whole by treating each and every apparatus, which is necessary for the functioning of the factory, as forming an integral part of the factory, known as "artificial silk manufacturing plant";

(2) Unless one apparatus, which independently is a plant or machine, when fitted to another machine to make that machine complete, becomes an integral part of the concerned asset itself and loses its independent identity, it cannot be said that the two assets exist. But, mere inter-dependency of each other for their functioning does not make two assets one for the purposes of claiming depreciation;

(3) Whatever rates are prescribed under sub-item (i) and (ii) of Part III of Appendix I in the first instance, depreciation has to be calculated at the rates as have been stated in column 2 of the table against each item and thereafter alone, the question of computing the extra shift allowance subject to the eligibility of each item of machinery or plant has to be considered;

(4) When air-conditioning machinery has been enlisted as a separate item of machinery or plant for the purposes of computation of rate of depreciation and it has also been enlisted for no extra shift allowance, it cannot be treated as artificial silk manufacturing machinery by treating it to be necessary part of the unit manufacturing artificial silk falling under that item unless it has become integral part of other machinery;

(5) It can be said that in the first instance the rate of general depreciation has to be prescribed under sub-item (i) and sub-item (ii) of the table and thereafter, when the question of extra shift allowance arises to be considered under sub-item (iv), it has to be seen what specific items have been excluded from the applicability of extra shift allowance and if any of the items has been specifically so excluded either by inscribing NESA while including that item under description of machinery and plant slated for special rate or are subjected to general rate, such item cannot be made available for computation of extra shift allowance.

There exists distinction between the description of air-conditioners as machinery used for manufacturing artificial silk and describing air-conditioners themselves as artificial silk manufacturing machinery or plant. The user of a particular machinery being essential for the use of another machinery or plant

itself does not make it a part of that machinery, to be treated as such. On this premise, the claim of air-conditioners fitted in wall which did not form an integral part of artificial silk machinery to extra shift allowance was not accepted.

Here also, it is apparent from the facts noticed above that exhaust fans, which are electrical machinery, about which there is no dispute, do not form an integral part of textile machinery, but fall in the category of electrical machinery used in textile factory. This alone is sufficient for rejecting the claim for extra shift allowance in the present case. The principle and the ratio in C.I.T. v. Kiran Crimpers (ITR 346 OF 1983, decided on 4th December, 1996) fully applies to the present case.

Accordingly, we answer question No.2 also in the negative, i.e. to say, in favour of the Revenue and against the assessee. There shall be no order as to costs.

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(apj)